AN ACT relating to the fiduciary duties owed to the state-administered retirement systems.

Be it enacted by the General Assembly of the Commonwealth of Kentucky:

➔Section 1. KRS 21.450 is amended to read as follows:

(1) The benefits provided by KRS 21.350 to 21.510 to be paid shall be funded through contract with a reputable life insurance company authorized to do business in this state, or through investment and reinvestment of funds in securities which, at the time of making the investment, are by law permitted for the investment of funds by fiduciaries in this state, or through a combination of such methods. To the extent that funding is provided through insurance contract, no contributions, payments or premiums shall be subject to any tax on insurance premiums or annuity considerations. The investment committee for the judicial retirement fund shall be trustee of any and all funds contributed or appropriated to the retirement system, and shall have sole authority to make insurance contracts or investments.

(2) (a) For the purposes of this subsection:

1. "Solely in the interest of the members and beneficiaries" shall be determined using only pecuniary factors and shall not include any purpose to further a nonpecuniary interest;

2. "Pecuniary factor" means a consideration having a direct and material connection to the financial risk or financial return of an investment;

3. A "material connection" is established if there is a substantial likelihood that a reasonable investor would consider it important in determining the financial risk or the financial return of an investment;

4. "Nonpecuniary interest" includes but is not limited to an environmental, social, political, or ideological interest which does not have a direct and material connection to the financial risk or financial return of an investment;~~[and]~~

5. "Investment manager" shall have the same definition attributed to "investment adviser" under the federal Investment Advisers Act of 1940, 15 U.S.C. sec. 80b-2***;***

6. "Shareholder-sponsored proposal" means a proposal by a shareholder included in the proxy statement of an issuer of securities pursuant to 17 C.F.R. sec. 240.14a-8; and

7. "Economic analysis" means a written analysis of the economic impact of a shareholder-sponsored proposal, which shall include, at a minimum:

a. The subject matter of the shareholder-sponsored proposal;

b. Whether the board of directors of the issuer of securities opposes the shareholder-sponsored proposal and the stated reasons for the opposition;

c. Whether the shareholder-sponsored proposal is consistent with the investment policy of the retirement system;

d. The economic benefits and costs of implementing the shareholder-sponsored proposal, as written, in the long and short term;

e. The quantifiable impact of the shareholder-sponsored proposal, as written, on the investment returns of the funds of the retirement system; and

f. An explanation of the modeling, procedures, and processes used to complete the economic analysis.

(b) The board members, any investment manager or other fiduciary, or proxy adviser shall discharge their duties with respect to the funds of the retirement system solely in the interest of the members and beneficiaries and:

1. For the exclusive purposes of providing benefits to members and their

beneficiaries and defraying reasonable expenses of administering the plan;

2. With the care, skill, prudence, and diligence under the circumstances then prevailing that a prudent person acting in a like capacity and familiar with such matters would use in the conduct of an enterprise of a like character and with like aims; and

3. In accordance with the federal, state, and common laws, regulations and other instruments governing the funds and fiduciaries.

(c) Evidence that a fiduciary has considered or acted on a nonpecuniary interest shall include but is not limited to:

1. Statements, explanations, reports, or correspondence;

2. Communications with portfolio companies;

3. Statements of principles or policies, whether made individually or jointly;

4. Votes of shares or proxies; or

5. Coalitions, initiatives, agreements, or commitments to which the fiduciary is a participant, affiliate, or signatory.

(d) When exercising or recommending a vote on a shareholder-sponsored proposal, a proxy adviser that has entered into an agreement or contracted with the board of trustees of the retirement system acts solely in the interest of the members and beneficiaries under this subsection if:

1. The proxy adviser's vote or recommendation is consistent with the recommendation of the board of directors of the issuer of the shares, provided:

a. The board of directors of the issuer of the shares is composed of a majority of independent directors; and

b. The recommendation of the board of directors is not for the

purpose of furthering a nonpecuniary interest; or

2. The proxy adviser's vote or recommendation is inconsistent with the recommendation of the board of directors of the issuer of the shares, provided the proxy adviser conducts and documents an economic analysis demonstrating that the vote or recommendation is solely in the interest of the members and beneficiaries.

(3) Any accrual of benefits provided under this or any other applicable statute shall be no less than the benefit adjustment provided for in KRS 21.405(4) from the date of the last establishment of that benefit.

(4) The board shall establish ethics policies and procedures by promulgation of administrative regulations in accordance with the provisions of KRS Chapter 13A. The ethics policies shall include but not be limited to annual financial and conflict of interest disclosure requirements which must be completed by all board members and made available to the public upon request.

(5) In addition to the standards of conduct prescribed by subsection (2) of this section:

(a) Investment managers shall comply with all applicable provisions of the Investment Advisers Act of 1940, as amended, and the rules and regulations promulgated thereunder, and shall comply with all other applicable federal securities statutes and related rules and regulations that apply to investment managers; and

(b) Proxy advisers and proxy voting services shall comply with all applicable provisions of the Investment Advisers Act of 1940, as amended, and the rules and regulations promulgated thereunder, and shall comply with all other federal statutes and related rules and regulations that apply to proxy advisers and proxy voting services.

(6) No contract or agreement, whether made in writing or not, shall in any manner waive, restrict, or limit a fiduciary's liability as to any of the duties imposed by this

section. Any agreement shall specify that it is made in the Commonwealth ***of Kentucky*** and governed by the laws of the Commonwealth ***of Kentucky***.

➔Section 2. KRS 61.650 is amended to read as follows:

(1) (a) The board shall be the trustee of funds created by KRS 16.510, 61.515, and 61.701 pertaining to the accounts for the Kentucky Employees Retirement System or State Police Retirement System, notwithstanding the provisions of any other statute to the contrary, and shall have exclusive power to invest and reinvest such assets in accordance with federal law.

(b) 1. The board shall establish an investment committee whose membership shall be composed of the following:

a. The three (3) trustees of the Kentucky Retirement Systems board appointed by the Governor pursuant to KRS 61.645 who have investment experience; and

b. Additional trustees appointed by the board chair.

2. The investment committee shall have authority to implement the investment policies adopted by the board and act on behalf of the board on all investment-related matters and to acquire, sell, safeguard, monitor, and manage the assets and securities of the several funds.

(c) 1. For the purposes of this paragraph:

a. "Solely in the interest of the members and beneficiaries" shall be determined using only pecuniary factors and shall not include any purpose to further a nonpecuniary interest;

b. "Pecuniary factor" means a consideration having a direct and material connection to the financial risk or financial return of an investment;

c. A "material connection" is established if there is a substantial likelihood that a reasonable investor would consider it important in determining the financial risk or the financial return of an investment;

d. "Nonpecuniary interest" includes but is not limited to an environmental, social, political, or ideological interest which does not have a direct and material connection to the financial risk or financial return of an investment;~~[and]~~

e. "Investment manager" shall have the same definition attributed to "investment adviser" under the federal Investment Advisers Act of 1940, 15 U.S.C. sec. 80b-2***;***

f. "Shareholder-sponsored proposal" means a proposal by a shareholder included in the proxy statement of an issuer of securities pursuant to 17 C.F.R. sec. 240.14a-8; and

g. "Economic analysis" means a written analysis of the economic impact of a shareholder-sponsored proposal, which shall include, at a minimum:

i. The subject matter of the shareholder-sponsored proposal;

ii. Whether the board of directors of the issuer of securities opposes the shareholder-sponsored proposal and the stated reasons for the opposition;

iii. Whether the shareholder-sponsored proposal is consistent with the investment policy of the retirement systems;

iv. The economic benefits and costs of implementing the shareholder-sponsored proposal, as written, in the long and short term;

v. The quantifiable impact of the shareholder-sponsored proposal, as written, on the investment returns of the funds of the retirement systems; and

vi. An explanation of the modeling, procedures, and processes used to complete the economic analysis.

2. A trustee, officer, employee, employee of the Kentucky Public Pensions Authority, investment manager, or other fiduciary, or proxy adviser shall discharge duties with respect to the retirement system:
   a. Solely in the interest of the members and beneficiaries;
   b. For the exclusive purpose of providing benefits to members and beneficiaries and paying reasonable expenses of administering the system;
   c. With the care, skill, and caution under the circumstances then prevailing that a prudent person acting in a like capacity and familiar with those matters would use in the conduct of an activity of like character and purpose;
   d. Impartially, taking into account any differing interests of members and beneficiaries;
   e. Incurring any costs that are appropriate and reasonable; and
   f. In accordance with a good-faith interpretation of the federal, state, and common law governing the system and fiduciaries.
3. Evidence that a fiduciary has considered or acted on a nonpecuniary interest shall include but is not limited to:
   a. Statements, explanations, reports, or correspondence;
   b. Communications with portfolio companies;
   c. Statements of principles or policies, whether made individually or jointly;
   d. Votes of shares or proxies; or
   e. Coalitions, initiatives, agreements, or commitments to which the fiduciary is a participant, affiliate, or signatory.

4. When exercising or recommending a vote on a shareholder-sponsored proposal, a proxy adviser that has entered into an agreement or contracted with the board of trustees of the retirement system acts solely in the interest of the members and beneficiaries under this subsection if:

a. The proxy adviser's vote or recommendation is consistent with the recommendation of the board of directors of the issuer of the shares, provided:

i. The board of directors of the issuer of the shares is composed of a majority of independent directors; and

ii. The recommendation of the board of directors is not for the purpose of furthering a nonpecuniary interest; or

b. The proxy adviser's vote or recommendation is inconsistent with the recommendation of the board of directors of the issuer of the shares, provided the proxy adviser conducts and documents an economic analysis demonstrating that the vote or recommendation is solely in the interest of the members and beneficiaries.

(d) In addition to the standards of conduct prescribed by paragraph (c) of this subsection:

1. All internal investment staff of the Kentucky Public Pensions Authority, and investment consultants shall adhere to the Code of Ethics and Standards of Professional Conduct, and all board trustees shall adhere to the Code of Conduct for Members of a Pension Scheme Governing Body. All codes cited in this subparagraph are promulgated by the CFA Institute;

2. Investment managers shall comply with all applicable provisions of the

federal Investment Advisers Act of 1940, as amended, and the rules and regulations promulgated thereunder, and shall comply with all other applicable federal securities statutes and related rules and regulations that apply to investment managers; and

3. Proxy advisers and proxy voting services shall comply with all applicable provisions of the Investment Advisers Act of 1940, as amended, and the rules and regulations promulgated thereunder, and shall comply with all other federal statutes and related rules and regulations that apply to proxy advisers and proxy voting services.

(e) No contract or agreement, whether made in writing or not, shall in any manner waive, restrict, or limit a fiduciary's liability as to any of the duties imposed by this section. Any agreement shall specify that it is made in the Commonwealth ***of Kentucky*** and governed by the laws of the Commonwealth ***of Kentucky***.

(2) The board, through adopted written policies, shall maintain ownership and control over its assets held in its unitized managed custodial account.

(3) The board, in keeping with its responsibility as trustee and wherever consistent with its fiduciary responsibilities, shall give priority to the investment of funds in obligation calculated to improve the industrial development and enhance the economic welfare of the Commonwealth.

(4) The contents of real estate appraisals, engineering or feasibility estimates, and evaluations made by or for the system relative to the acquisition or disposition of property, until such time as all of the property has been acquired or sold, shall be excluded from the application of KRS 61.870 to 61.884 and shall be subject to inspection only upon order of a court of competent jurisdiction.

(5) Based upon market value at the time of purchase, the board shall limit the amount of assets managed by any one (1) active or passive investment manager to fifteen

percent (15%) of the assets in the pension and insurance funds.

(6) All contracts for the investment or management of assets of the systems shall not be subject to KRS Chapters 45, 45A, 56, and 57. Instead, the board shall conduct the following process to develop and adopt an investment procurement policy with which all prospective contracts for the investment or management of assets of the systems shall comply:

(a) On or before July 1, 2017, the board shall consult with the secretary of the Finance and Administration Cabinet or his or her designee to develop an investment procurement policy, which shall be written to meet best practices in investment management procurement;

(b) Thirty (30) days prior to adoption, the board shall tender the preliminary investment procurement policy to the secretary of the Finance and Administration Cabinet or his or her designee for review and comment;

(c) Upon receipt of comments from the secretary of the Finance and Administration Cabinet or his or her designee, the board shall choose to adopt or not adopt any recommended changes;

(d) Upon adoption, the board shall tender the final investment procurement policy to the secretary of the Finance and Administration Cabinet or his or her designee;

(e) No later than thirty (30) days after receipt of the investment procurement policy, the secretary or his or her designee shall certify whether the board's investment procurement policy meets or does not meet best practices for investment management procurement; and

(f) Any amendments to the investment procurement policy shall adhere to the requirements set forth by paragraphs (b) to (e) of this subsection.

(7) (a) The board shall adopt written proxy voting guidelines which are consistent with the fiduciary duties and other requirements of this section.

(b) The board shall not adopt the recommendations of a proxy adviser or proxy voting service and shall not allow such proxy adviser or proxy voting service to vote on behalf of the system, unless the proxy adviser or proxy voting service acknowledges in writing and accepts under contract its duties under this section and commits to follow the board-adopted proxy voting guidelines when voting the system's shares in order to comply with the board's fiduciary duties and other responsibilities under this section.

(c) All shares held by or on behalf of the system, and which the system is entitled to vote under state, federal, or common laws, shall be voted according to the proxy voting guidelines adopted by the board and subject to the fiduciary duties and other requirements of this section by:

1. The board, the investment committee of the board, or an employee or employees of the Authority who are fiduciaries under subsection (1) of this section and are appointed or otherwise authorized by the board; or
2. A proxy adviser or proxy voting service that acknowledges in writing and accepts under contract its duties under this section and commits to follow the board-adopted proxy voting guidelines when voting the system's shares in order to comply with the board's fiduciary duties and other responsibilities under this section.

(d) All proxy votes shall be reported at least quarterly to the board. For each vote, the report shall provide:

1. The vote caption;
2. The date of the vote;
3. The company's name;
4. The vote cast for the system;
5. The recommendation of the company's management; and
6. If applicable, the recommendation of the proxy adviser or proxy voting

service.

➔Section 3. KRS 78.790 is amended to read as follows:

(1) (a) The board shall be the trustee of funds pertaining to the County Employees Retirement System created by KRS 78.510 to 78.852, and KRS 61.701, and shall have full and exclusive power to invest and reinvest such assets in accordance with federal law.

(b) 1. The board shall establish an investment committee that shall include members of the board with investment experience, elected members, or other members as determined by the board chair, and may also include nonvoting members who have investment expertise.

2. The investment committee shall have authority to implement the investment policies adopted by the board and act on behalf of the board on all investment-related matters.

(c) 1. For the purposes of this paragraph:

a. "Solely in the interest of the members and beneficiaries" shall be determined using only pecuniary factors and shall not include any purpose to further a nonpecuniary interest;

b. "Pecuniary factor" means a consideration having a direct and material connection to the financial risk or financial return of an investment;

c. A "material connection" is established if there is a substantial likelihood that a reasonable investor would consider it important in determining the financial risk or the financial return of an investment;

d. "Nonpecuniary interest" includes but is not limited to an environmental, social, political, or ideological interest which does not have a direct and material connection to the financial risk or financial return of an investment;~~[and]~~

e. "Investment manager" shall have the same definition attributed to "investment adviser" under the federal Investment Advisers Act of 1940, 15 U.S.C. sec. 80b-2***;***

f. "Shareholder-sponsored proposal" means a proposal by a shareholder included in the proxy statement of an issuer of securities pursuant to 17 C.F.R. sec. 240.14a-8; and

g. "Economic analysis" means a written analysis of the economic impact of a shareholder-sponsored proposal, which shall include, at a minimum:

i. The subject matter of the shareholder-sponsored proposal;

ii. Whether the board of directors of the issuer of securities opposes the shareholder-sponsored proposal and the stated reasons for the opposition;

iii. Whether the shareholder-sponsored proposal is consistent with the investment policy of the retirement system;

iv. The economic benefits and costs of implementing the shareholder-sponsored proposal, as written, in the long and short term;

v. The quantifiable impact of the shareholder-sponsored proposal, as written, on the investment returns of the funds of the retirement system; and

vi. An explanation of the modeling, procedures, and processes used to complete the economic analysis.

2. A trustee, officer, employee, employee of the Kentucky Public Pensions Authority, investment manager, or other fiduciary, or proxy adviser shall discharge duties with respect to the system:

a. Solely in the interest of the members and beneficiaries;

b. For the exclusive purpose of providing benefits to members and beneficiaries and paying reasonable expenses of administering the system;

c. With the care, skill, and caution under the circumstances then prevailing that a prudent person acting in a like capacity and familiar with those matters would use in the conduct of an activity of like character and purpose;

d. Impartially, taking into account any differing interests of members and beneficiaries;

e. Incurring any costs that are appropriate and reasonable; and

f. In accordance with a good-faith interpretation of the federal, state, and common law governing the system and fiduciaries.

3. Evidence that a fiduciary has considered or acted on a nonpecuniary interest shall include but is not limited to:

a. Statements, explanations, reports, or correspondence;

b. Communications with portfolio companies;

c. Statements of principles or policies, whether made individually or jointly;

d. Votes of shares or proxies; or

e. Coalitions, initiatives, agreements, or commitments to which the fiduciary is a participant, affiliate, or signatory.

4. When exercising or recommending a vote on a shareholder-sponsored proposal, a proxy adviser that has entered into an agreement or contracted with the board of trustees of the retirement system acts solely in the interest of the members and beneficiaries under this subsection if:

a. The proxy adviser's vote or recommendation is consistent with the recommendation of the board of directors of the issuer of the shares, provided:

i. The board of directors of the issuer of the shares is composed of a majority of independent directors; and

ii. The recommendation of the board of directors is not for the purpose of furthering a nonpecuniary interest; or

b. The proxy adviser's vote or recommendation is inconsistent with the recommendation of the board of directors of the issuer of the shares, provided the proxy adviser conducts and documents an economic analysis demonstrating that the vote or recommendation is solely in the interest of the members and beneficiaries.

(d) In addition to the standards of conduct prescribed by paragraph (c) of this subsection:

1. All internal investment staff of the Kentucky Public Pensions Authority, and investment consultants shall adhere to the Code of Ethics and Standards of Professional Conduct, and all board trustees shall adhere to the Code of Conduct for Members of a Pension Scheme Governing Body. All codes cited in this subparagraph are promulgated by the CFA Institute;

2. Investment managers shall comply with all applicable provisions of the federal Investment Advisers Act of 1940, as amended, and the rules and regulations promulgated thereunder, and shall comply with all other applicable federal securities statutes and related rules and regulations that apply to investment managers; and

3. Proxy advisers and proxy voting services shall comply with all

applicable provisions of the Investment Advisers Act of 1940, as amended, and the rules and regulations promulgated thereunder, and shall comply with all other federal statutes and related rules and regulations that apply to proxy advisers and proxy voting services.

(e) No contract or agreement, whether made in writing or not, shall in any manner waive, restrict, or limit a fiduciary's liability as to any of the duties imposed by this section. Any agreement shall specify that it is made in the Commonwealth and governed by the laws of the Commonwealth.

(2) The board, through adopted written policies, shall maintain ownership and control over its assets held in its unitized managed custodial account.

(3) The board, in keeping with its responsibility as the trustee and wherever feasible, shall give priority to the investment of funds in obligations calculated to improve the industrial development and enhance the economic welfare of the Commonwealth.

(4) The contents of real estate appraisals, engineering or feasibility estimates, and evaluations made by or for the system relative to the acquisition or disposition of property, until such time as all of the property has been acquired or sold, shall be excluded from the application of KRS 61.870 to 61.884 and shall be subject to inspection only upon order of a court of competent jurisdiction.

(5) Based upon market value at the time of purchase, the board shall limit the amount of assets managed by any one (1) active or passive investment manager to fifteen percent (15%) of the assets in the pension and insurance funds.

(6) All contracts for the investment or management of assets of the system shall not be subject to KRS Chapters 45, 45A, 56, and 57. Instead, the board shall conduct the following process to develop and adopt an investment procurement policy with which all prospective contracts for the investment or management of assets of the system shall comply:

(a) The board shall consult with the secretary of the Finance and Administration Cabinet or his or her designee to develop an investment procurement policy, which shall be written to meet best practices in investment management procurement;

(b) Thirty (30) days prior to adoption, the board shall tender the preliminary investment procurement policy to the secretary of the Finance and Administration Cabinet or his or her designee for review and comment;

(c) Upon receipt of comments from the secretary of the Finance and Administration Cabinet or his or her designee, the board shall choose to adopt or not adopt any recommended changes;

(d) Upon adoption, the board shall tender the final investment procurement policy to the secretary of the Finance and Administration Cabinet or his or her designee;

(e) No later than thirty (30) days after receipt of the investment procurement policy, the secretary or his or her designee shall certify whether the board's investment procurement policy meets or does not meet best practices for investment management procurement; and

(f) Any amendments to the investment procurement policy shall adhere to the requirements set forth by paragraphs (b) to (e) of this subsection.

(7) (a) The board shall adopt written proxy voting guidelines, which are consistent with the fiduciary duties and other requirements of this section.

(b) The board shall not adopt the recommendations of a proxy adviser or proxy voting service and shall not allow such proxy adviser or proxy voting service to vote on behalf of the system, unless the proxy adviser or proxy voting service acknowledges in writing and accepts under contract its duties under this section and commits to follow the board-adopted proxy voting guidelines when voting the system's shares in order to comply with the board's fiduciary duties and other responsibilities under this section.

(c) All shares held by or on behalf of the system, and which the system is entitled to vote under state, federal, or common laws, shall be voted according to the proxy voting guidelines adopted by the board and subject to the fiduciary duties and other requirements of this section by:

1. The board, the investment committee of the board, or an employee or employees of the Authority who are fiduciaries under subsection (1) of this section and are appointed or otherwise authorized by the board; or

2. A proxy adviser or proxy voting service that acknowledges in writing and accepts under contract its duties under this section and commits to follow the board-adopted proxy voting guidelines when voting the system's shares in order to comply with the board's fiduciary duties and other responsibilities under this section.

(d) All proxy votes shall be reported at least quarterly to the board. For each vote, the report shall provide:

1. The vote caption;
2. The date of the vote;
3. The company's name;
4. The vote cast for the system;
5. The recommendation of the company's management; and
6. If applicable, the recommendation of the proxy adviser or proxy voting service.

➔Section 4. KRS 161.430 is amended to read as follows:

(1) (a) The board of trustees shall be the trustee of the funds of the retirement system and shall have full power and responsibility for the purchase, sale, exchange, transfer, or other disposition of the investments and moneys of the retirement system. The board shall, by administrative regulation, establish investment

policies and procedures to carry out their responsibilities.

(b) 1. The board shall contract with experienced competent investment managers to invest and manage assets of the system. The board may also employ qualified investment staff to advise it on investment matters and to invest and manage assets of the system not to exceed fifty percent (50%) of the system's assets. The board may contract with one (1) or more general investment consultants, as well as specialized investment consultants, to advise it on investment matters.

2. All internal investment staff and investment consultants shall adhere to the Code of Ethics and Standards of Professional Conduct, and all board trustees shall adhere to the Code of Conduct for Members of a Pension Scheme Governing Body, promulgated by the CFA Institute. Investment managers shall comply with the federal Investment Advisers Act of 1940, as amended, and the rules and regulations promulgated thereunder and shall comply with all other applicable federal securities statutes and related rules and regulations that apply to investment managers.

3. No investment manager shall manage more than forty percent (40%) of the funds of the retirement system.

(c) The board may appoint an investment committee to act for the board in all matters of investment, subject to the approval of the board of trustees. The board of trustees, in keeping with their responsibilities as trustees and wherever consistent with their fiduciary responsibilities, shall give priority to the investment of funds in obligations calculated to improve the industrial development and enhance the economic welfare of the Commonwealth. Toward this end, the board shall develop procedures for informing the business community of the potential for in-state investments by the retirement fund, accepting and evaluating applications for the in-state investment of funds, and working with members of the business community in executing in-state investments which are consistent with the board's fiduciary responsibilities. The board shall include in the criteria it uses to evaluate in-state investments their potential for creating new employment opportunities and adding to the total job pool in Kentucky. The board may cooperate with the board of trustees of Kentucky Retirement Systems in developing its program and procedures, and shall report to the Legislative Research Commission annually on its progress in placing in-state investments. The first report shall be submitted by October 1, 1991, and subsequent reports shall be submitted by October 1 of each year thereafter. The report shall include the number of applications for in-state investment received, the nature of the investments proposed, the amount requested, the amount invested, and the percentage of applications which resulted in investments.

(2) (a) For the purposes of this subsection:

1. "Solely in the interest of the members and ***annuitants***~~[beneficiaries]~~" shall be determined using only pecuniary factors and shall not include any purpose to further a nonpecuniary interest;

2. "Pecuniary factor" means a consideration having a direct and material connection to the financial risk or financial return of an investment;

3. A "material connection" is established if there is a substantial likelihood that a reasonable investor would consider it important in determining the financial risk or the financial return of an investment;

4. "Nonpecuniary interest" includes but is not limited to an environmental, social, political, or ideological interest which does not have a direct and material connection to the financial risk or financial return of an investment;~~[and]~~

5. "Investment manager" and "investment consultant" shall have the same

definition attributed to "investment adviser" under the federal Investment Advisers Act of 1940, 15 U.S.C. sec. 80b-2**;**

6. Shareholder-sponsored proposal" means a proposal by a shareholder included in the proxy statement of an issuer of securities pursuant to 17 C.F.R. sec. 240.14a-8; and

7. "Economic analysis" means a written analysis of the economic impact of a shareholder-sponsored proposal, which shall include, at a minimum:

a. The subject matter of the shareholder-sponsored proposal;

b. Whether the board of directors of the issuer of securities opposes the shareholder-sponsored proposal and the stated reasons for the opposition;

c. Whether the shareholder-sponsored proposal is consistent with the investment policy of the retirement system;

d. The economic benefits and costs of implementing the shareholder-sponsored proposal, as written, in the long and short term;

e. The quantifiable impact of the shareholder-sponsored proposal, as written, on the investment returns of the funds of the retirement system; and

f. An explanation of the modeling, procedures, and processes used to complete the economic analysis.

(b) The board members, investment managers, investment consultants, or other fiduciaries, and proxy advisers shall discharge their duties with respect to the assets of the system solely in the interests of the active contributing members and annuitants and:

1. For the exclusive purpose of providing benefits to members and

annuitants and defraying reasonable expenses of administering the system;

2. With the care, skill, prudence, and diligence under the circumstances then prevailing that a prudent person acting in a like capacity and familiar with these matters would use in the conduct of an enterprise of a like character and with like aims;

3. By diversifying the investments of the plan so as to minimize the risk of large losses, unless under the circumstances it is clearly prudent not to do so; and

4. In accordance with the federal, state, and common laws, administrative regulations, and other instruments governing the system and fiduciaries.

(c) Evidence that a fiduciary has considered or acted on a nonpecuniary interest shall include but is not limited to:

1. Statements, explanations, reports, or correspondence;

2. Communications with portfolio companies;

3. Statements of principles or policies, whether made individually or jointly;

4. Votes of shares or proxies; or

5. Coalitions, initiatives, agreements, or commitments to which the fiduciary is a participant, affiliate, or signatory.

(d) When exercising or recommending a vote on a shareholder-sponsored proposal, a proxy adviser that has entered into an agreement or contracted with the board of trustees of the retirement system acts solely in the interest of the members and annuitants under this subsection if:

1. The proxy adviser's vote or recommendation is consistent with the recommendation of the board of directors of the issuer of the shares, provided:

a. The board of directors of the issuer of the shares is composed of a majority of independent directors; and

b. The recommendation of the board of directors is not for the purpose of furthering a nonpecuniary interest; or

2. The proxy adviser's vote or recommendation is inconsistent with the recommendation of the board of directors of the issuer of the shares, provided the proxy adviser conducts and documents an economic analysis demonstrating that the vote or recommendation is solely in the interest of the members and annuitants.

(3) (a) In choosing and contracting for professional investment management and consulting services, the board shall do so prudently and in the interest of the members and annuitants. Any contract that the board makes with an investment manager shall set forth policies and guidelines of the board with reference to standard rating services and specific criteria for determining the quality of investments. Expenses directly related to investment management and consulting services shall be financed from the guarantee fund in amounts approved by the board.

(b) An investment manager or consultant appointed under this section shall acknowledge in writing his or her fiduciary responsibilities to the fund. To be eligible for appointment, an investment manager, consultant, or an affiliate, shall be:

1. Registered under the Federal Investment Advisers Act of 1940; or

2. A bank as defined by that Act; or

3. An insurance company qualified to perform investment services under the laws of more than one (1) state.

(c) Proxy advisers and proxy voting services shall comply with all applicable provisions of the Investment Advisers Act of 1940, as amended, and the rules and regulations promulgated thereunder, and shall comply with all other federal statutes and related rules and regulations that apply to proxy advisers and proxy voting services.

(d) No contract or agreement, whether made in writing or not, shall in any manner waive, restrict, or limit a fiduciary's liability as to any of the duties imposed by this section. Any agreement shall specify that it is made in the Commonwealth ***of Kentucky*** and governed by the laws of the Commonwealth ***of Kentucky***.

(4) No investment or disbursement of funds shall be made unless authorized by the board of trustees, except that the board, in order to ensure timely market transactions, shall establish investment guidelines and may permit its staff and investment managers who are employed or under contract with the board pursuant to this section to execute purchases and sales of investment instruments within those guidelines without prior board approval.

(5) In discharging his or her administrative duties under this section, a trustee shall strive to administer the retirement system in an efficient and cost-effective manner for the taxpayers of the Commonwealth of Kentucky.

(6) Notwithstanding any other provision of KRS 161.220 to 161.716, no funds of the Teachers' Retirement System, including fees and commissions paid to an investment manager, private fund, or company issuing securities, who manages systems assets, shall be used to pay fees and commissions to placement agents. For purposes of this subsection, "placement agent" means a third-party individual, who is not an employee, or firm, wholly or partially owned by the entity being hired, who solicits investments on behalf of an investment manager, private fund, or company issuing securities.

(7) All contracts for the investment or management of assets of the system shall not be subject to KRS Chapters 45, 45A, 56, and 57. Instead, the board shall conduct the

following process to develop and adopt an investment procurement policy with which all prospective contracts for the investment or management of assets of the system shall comply:

(a) On or before July 1, 2017, the board shall consult with the secretary of the Finance and Administration Cabinet or his or her designee to develop an investment procurement policy, which shall be written to meet best practices in investment management procurement;

(b) Thirty (30) days prior to adoption, the board shall tender the preliminary investment procurement policy to the secretary of the Finance and Administration Cabinet or his or her designee for review and comment;

(c) Upon receipt of comments from the secretary of the Finance and Administration Cabinet or his or her designee, the board shall choose to adopt or not adopt any recommended changes;

(d) Upon adoption, the board shall tender the final investment procurement policy to the secretary of the Finance and Administration Cabinet or his or her designee;

(e) No later than thirty (30) days after receipt of the investment procurement policy, the secretary or his or her designee shall certify whether the board's investment procurement policy meets or does not meet best practices for investment management procurement; and

(f) Any amendments to the investment procurement policy shall adhere to the requirements set forth by paragraphs (b) to (e) of this subsection.

(8) (a) The board shall adopt written proxy voting guidelines which are consistent with the fiduciary duties and other requirements of this section.

(b) The board shall not adopt the recommendations of a proxy adviser or proxy voting service and shall not allow such proxy adviser or proxy voting service to vote on behalf of the system, unless the proxy adviser or proxy voting service acknowledges in writing and accepts under contract its duties under this section and commits to follow the board-adopted proxy voting guidelines when voting the system's shares in order to comply with the board's fiduciary duties and other responsibilities under this section.

(c) All shares held by or on behalf of the system, and which the system is entitled to vote under state, federal, or common laws, shall be voted according to the proxy voting guidelines adopted by the board and subject to the fiduciary duties and other requirements of this section by:

1. The board, the investment committee of the board, or an employee or employees of the system who are fiduciaries under this section and are appointed or otherwise authorized by the board; or
2. A proxy adviser or proxy voting service that acknowledges in writing and accepts under contract its duties under this section and commits to follow the board-adopted proxy voting guidelines when voting the system's shares in order to comply with the board's fiduciary duties and other responsibilities under this section.

(d) All proxy votes shall be reported at least quarterly to the board. For each vote, the report shall provide:

1. The vote caption;
2. The date of the vote;
3. The company's name;
4. The vote cast for the system;
5. The recommendation of the company's management; and
6. If applicable, the recommendation of the proxy adviser or proxy voting service.